

The Procter & Gamble Company

1986 Annual Report





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EDWIN L. ARTZT	<i>Vice Chairman of the Board and President, Procter & Gamble International</i>
THEODORE F. BROPHY	<i>Chairman and Chief Executive Officer GTE Corporation — telecommunications, electrical and electronic products, services and systems</i>
GERALD V. DIRVIN	<i>Group Vice President</i>
CHARLES T. DUNCAN	<i>Partner in the law firm of Reid & Priest, Washington, D.C.</i>
RICHARD J. FERRIS	<i>Chairman, President and Chief Executive Officer UAL, Inc. — travel related services</i>
ROBERT A. HANSON	<i>Chairman and Chief Executive Officer Deere & Company — agricultural and industrial equipment</i>
THOMAS LACO	<i>Vice Chairman of the Board</i>
JOSHUA LEDERBERG	<i>President The Rockefeller University</i>
WALTER F. LIGHT	<i>Retired Chairman Northern Telecom Limited telecommunications equipment and services</i>
JAMES W. NETHERCOTT	<i>Senior Vice President</i>
JOHN E. PEPPER	<i>President</i>
DAVID M. RODERICK	<i>Chairman of the Board and Chief Executive Officer USX Corporation energy, steel and other manufacturing</i>
JOHN S. SCOTT	<i>President and Chief Executive Officer Richardson-Vicks Inc., a subsidiary of the Company</i>
JOHN G. SMALE	<i>Chairman of the Board and Chief Executive</i>
DAVID S. SWANSON	<i>Senior Vice President</i>
MARINA v.N. WHITMAN	<i>Vice President and Group Executive General Motors Corporation automobiles and related equipment</i>

JOHN G. SMALE	<i>Chairman of the Board and Chief Executive</i>
EDWIN L. ARTZT	<i>Vice Chairman of the Board and President, Procter & Gamble International</i>
THOMAS LACO	<i>Vice Chairman of the Board</i>
JOHN E. PEPPER	<i>President</i>

Senior Vice Presidents

W. WALLACE ABBOTT
 ALBERT E. HARRIS
 POWELL McHENRY — *General Counsel*
 JAMES W. NETHERCOTT
 DAVID S. SWANSON
 HARRY TECKLENBURG
 WAHIB N. ZAKI

Group Vice Presidents

ROBERT E. CANNON
 GERALD V. DIRVIN
 STEPHEN P. DONOVAN, JR.
 HARALD EINSMANN
 B. JURGEN HINTZ (elected July 8, 1986)
 MALCOLM JOZOFF
 SAMIH A. SHERIF

Vice Presidents

J. RICHARD ANDRE
Research and Development

WOLFGANG C. BERNDT
*International, Western Hemisphere
 and the Philippines*

BENJAMIN L. BETHELL
*Manufacturing, Engineering
 and Purchases, Europe*

ROBERT T. BLANCHARD
Beverage Division

GARY E. BOOTH
Research and Development

CHARLES D. BROADDUS
Research

GORDON F. BRUNNER
Research and Development

CHARLES C. CARROLL
*Bar Soap and Household Cleaning
 Products Division*

WILLIAM O. COLEMAN
Professional Relations

WILLIAM B. CONNELL
Beauty Care Division

T. MARSHALL COURTNEY
Cellulose and Specialties Division

EDWIN H. EATON, JR.
Treasurer

STONA J. FITCH
Manufacturing, U.S.

GEORGE M. GIBSON
Comptroller

ROBERT V. GOLDSTEIN
Advertising

ROY W. R. KENDALL
Canada

CHARLES A. LIEPPE
Health and Personal Care Division

LAWRENCE D. MILLIGAN
Food Products Division

RICHARD R. NICOLosi
Paper Products Division

GEOFFREY PLACE
Research and Development

LOUIS A. PRITCHETT
Sales

SAMUEL H. PRUETT
Personnel

R. MARVIN WOMACK
Purchases

Secretary

ASHLEY L. FORD

Richardson-Vicks Inc.

JOHN S. SCOTT
 WILLIAM I. BERGMAN
 JOHN R. MARKLEY
 LOUIS P. MATTIS
 IVAN HUSOVSKY

President and Chief Executive Officer
Executive Vice President
Executive Vice President
Executive Vice President
Senior Vice President



Left to right are Thomas Laco, John G. Smale, John E. Pepper and Edwin L. Artzt.

To Our Shareholders:

Financial Highlights

We submit herewith the Annual Report of The Procter & Gamble Company for the 1986 fiscal year which ended June 30, 1986.

Net sales for the year amounted to \$15.4 billion, an increase of 14% over net sales of \$13.5 billion for the previous year.

Net earnings amounted to \$709 million, an increase of 12% over net earnings of \$635 million for the preceding year. Earnings per share were \$4.20 which compares with \$3.80 for the previous year. The growth in net earnings was held back by both a higher effective income tax rate versus the previous year and the initial dilution effect of two major acquisitions.

Dividends of \$2.625 per common share were paid during the year. The comparable amount for the previous year was \$2.60 per share. Effective with the May, 1986, payment, the quarterly dividend was increased to an annual rate of \$2.70 per share. This marked the 30th consecutive fiscal year of increased dividend payments.

This past year's profit recovery was in line with our expectations following the heavy investment in both new products and key established brands. Significant progress was made in several major product categories in the United States, and the two acquisitions considerably increased our presence in the health and beauty aids business.

Acquisitions

In November, 1985, Richardson-Vicks Inc., a worldwide manufacturer and marketer of personal care products, was acquired for \$1.2 billion. Richardson-Vicks, which is now operating as a wholly-owned subsidiary, includes such leading brands as the Vicks line of cold products, Oil of Olay and Clearasil skin care products, and Vidal Sassoon hair care products. We have already begun to realign responsibilities for some similar P&G and RVI products among Richardson-Vicks and several other Company operating units in order to achieve greater integration and efficiencies in the United States and abroad. Beginning on page 10 of this report is a pictorial essay on this important acquisition which is the largest in the history of the Company.

In December, 1985, the Company acquired the over-the-counter drug business of G.D. Searle & Co. for \$312 million. This included Metamucil, the leading laxative product in the United States. Together with our existing health and personal care and beauty care divisions, these acquisitions will enhance our position as a worldwide leader of health and beauty aids.

**United
States
Business**

A new domestic consumer unit volume record was established this year apart from the additional volume from the Richardson-Vicks and Searle acquisitions. Domestic net earnings from operations totaled \$634 million, an increase of 22% over the previous year. The acquisitions had virtually no impact on domestic net earnings.

Particularly encouraging was the significant growth achieved in several core product categories which form a major part of the domestic business:

- In the disposable diaper category, shipment volume and market share moved ahead strongly following the major product technology changes made over the past two years. Today, diaper market share is significantly higher than it was a year ago and we have increased our market leadership position.
- We significantly improved market share and our position as dentifrice market leader, led by strong consumer acceptance of new Crest Tartar Control Formula toothpaste. The new Crest push-button, pump package was also expanded broadly in all four product formulas: regular, mint, gel and tartar control.
- In the highly competitive laundry detergent category, the volume and market share growth of Liquid Tide, and the expansion to national distribution of Liquid Bold-3, have given the Company market leadership in the liquids segment of this category. This success has been accompanied by overall growth in the Company's laundry detergent business, a category in which we have long held the position of market leader.

Additional product and packaging improvements highlighted efforts in several of the new product categories we had entered the past few years:

- In the feminine sanitary pads category, Always Plus, an improved product offering more protection, was expanded nationally this past May. This innovative product should strengthen the market position of Always, which currently is the number two brand in the marketplace.
- Citrus Hill orange juice increased volume significantly this past year following the expansion late in the previous year of improved Citrus Hill Select.
- Duncan Hines cookies now hold the number one market share position in the soft cookie category. However, our share of the market has been reduced because of patent infringement by competitors, a matter that the Company continues to pursue in U.S. District Court. Recently, new initiatives — improvements in both packaging and product — have been placed in national distribution.

Elsewhere, a number of new companion products to existing Company brands were expanded this past year to national distribution. These included Mr. Clean Cleanser, a liquid, soft abrasive cleanser; a new Bakery Style version of our popular Duncan Hines Muffin Mixes; a new unscented version of Ivory Shampoo and Ivory Conditioner; a new, wide-solid form of Sure anti-perspirant; and a new powder-fresh scent of Secret anti-perspirant. In addition, Richardson-Vicks introduced broadly our first hair coloring product, Vidal Sassoon Colorific, available in both mousse and gel.

International Operations

International operations contributed \$143 million to net earnings, an increase of 49% from the previous year. These results were principally due to the addition of the Richardson-Vicks international business, although existing business growth and currency exchange rates were also positive factors.

Established business results were particularly strong in the European laundry detergent category, reflecting share growth across all subsidiaries. In Japan, after many difficult years in this very competitive market, unit volume improved sharply on the strength of a new Pampers product and significant marketing investment behind improved detergent products. Less favorable results were experienced in Latin America, however, as cost inflation in excess of government-allowed pricing resulted in significantly lower operating margins.

Investments in new products, quality improvements in established products and activity in new geographic markets continued at high levels during this past year. A significant number of new products were expanded in Europe, including Mr. Proper household scouring cream in several subsidiaries, Spic & Span Liquid in Italy and Flash Liquid in the United Kingdom. Elsewhere, new versions of Pampers were introduced into several key markets and, in the United Kingdom and Canada, Crest Tartar Control Formula generated solid business growth. In the Middle East, unit volume advanced despite a reduced level of economic activity in this oil producing region. In Egypt, plans for a joint venture are progressing satisfactorily.

We continue to make significant marketing investments in the Far East. Although economic growth in a number of these markets has recently slowed, the Company remains committed to an expanded presence in this area. We are particularly encouraged by the opportunities afforded by the Richardson-Vicks acquisition, which will provide a more substantial base for continuing and expanding operations in these markets.

Continuing Financial Strength

The Company increased long-term debt by \$1.6 billion during the past year with the proceeds used primarily to fund the acquisition of Richardson-Vicks and the Searle over-the-counter drug business. Additional capital was provided by a new, variable rate preferred stock issue amounting to \$250 million.

Despite these increases in debt and equity capital, the Company's debt to total capital employed remains at a healthy level. After these borrowings, the Company's financial credit ratings remain strong, which are evidence of its continuing financial strength.

Capital Expenditures

Capital expenditures totaled \$1.1 billion, or about the same level as last year. Product improvements in our existing business provided the impetus for more than a third of these expenditures and included continuing projects to improve our diaper technology throughout the world. Cost savings and new capacity projects also contributed significantly to new capital investment. In the coming year, we anticipate that expenditures will remain near current levels with continuing emphasis on product improvements, cost savings and new capacity projects.

**Research
and
Development**

The lifeblood of the Company's growth through the years has been the continuing flow of new and improved products developed by our research organization. Last year, research and development expenses on both new products and existing products totaled \$479 million, and our commitment to these activities will continue in the years ahead.

**Tax
Reform**

As this Report goes to press, a joint Senate-House conference committee is reviewing proposed legislation to revise and to simplify the federal income tax code. We support this milestone effort for tax reform. Initially, both the Senate and the House versions would increase the Company's taxes since the loss of tax incentive items such as the investment tax credit would precede the reduction in the corporate tax rate. After the initial year, however, the Company should benefit from what is a more equitable tax code.

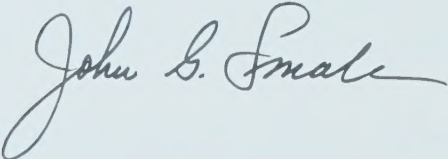
**Owen B.
Butler**

On March 31, 1986, Brad Butler retired from the Company after serving as Chairman of the Board since 1981. His contributions to the Company go well beyond his considerable impact on the growth of the business in the more than forty years he was an employee. His dedication, his high principles, his regard for his fellow employees and his sense of responsibility as a citizen have been strong motivation for all who knew him. He has left his mark both inside and outside the Company. We will greatly miss him.

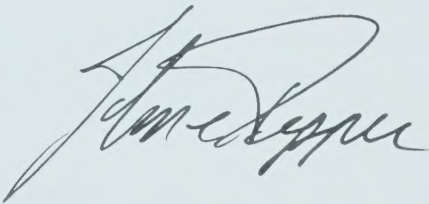
Our continuing progress is due importantly to the dedication and vitality of the 74,000 men and women of Procter & Gamble — including now the 10,000 employees of Richardson-Vicks. It is their efforts and talents that will drive the business ahead.

On June 27, 1986, Sanford G. Weiner, Group Vice President of Procter & Gamble, died following an extended illness. His untimely death at the age of forty-six removed from our senior managerial ranks an outstanding businessman and a compassionate person whose energy, strength of character, and deep interest in others enriched all of us.

Respectfully,



Chairman of the Board and Chief Executive



President

August 8, 1986

The following changes were made in the senior management and Board of Directors of the Company during the past year:

Owen B. Butler, Chairman of the Board, retired as an officer and director of the Company on March 31, 1986 after a distinguished career spanning forty years.

John G. Smale, previously President and Chief Executive officer, was elected Chairman of the Board. He will continue as Chief Executive officer of the Company.

John E. Pepper was elected President of the Company. He was previously Executive Vice President.

Stephen P. Donovan, Jr. was elected Group Vice President with responsibility for the Bar Soap and Household Cleaning Products and Packaged Soap and Detergent Divisions. He was previously Vice President-Packaged Soap and Detergent Division.

B. Jurgen Hintz was elected Group Vice President with responsibility for the Beverage and Food Products Divisions and for Crush Products and Soft Drink Bottling. He was previously Vice President-Beverage Division.

Amory Houghton, Jr., Chairman of the Executive Committee of Corning Glass Works, resigned from the Board of Directors to run for Congress in New York. He had served with distinction as a director since 1978.

John S. Scott, President and Chief Executive Officer, Richardson-Vicks Inc., was elected to the Board of Directors.

The following vice presidents announced their retirement last year:

James M. Edwards, Vice President-Manufacturing, International, retired June 30, 1986, after more than thirty-seven years of capable service.

J. Russell Marsden, Vice President, retired for reasons of health on June 30, 1986, after nearly thirty years of dedicated service.

William D. McHardy, Vice President-Disposable Products, Europe, retired on June 30, 1986, after thirty-six years of productive service.

The following new vice presidents were elected during the past year:

J. Richard Andre, Vice President — Research and Development

Gary E. Booth, Vice President — Research and Development

Gordon F. Brunner, Vice President — Research and Development

Richard R. Nicolosi, Vice President — Paper Products Division

Richardson-Vicks and P&G: Forging An Exciting Future

The largest acquisition in Procter & Gamble's history was completed in late 1985 with the purchase of Richardson-Vicks Inc. (RVI). RVI employs 10,000 people and had worldwide sales of \$1.3 billion for fiscal year 1985. This acquisition is an important step for P&G in achieving a basic strategic objective of increasing its worldwide business in the health and personal care fields.

Brand Leaders

Richardson-Vicks is a company of many leading brands. It is the long-term leading producer of cough and cold products with the Vicks line of cold care medicines. Its denture adhesive products, Fasteeth and Fixodent, are top sellers. RVI also enjoys worldwide leadership in the facial moisturizer and acne treatment categories with the Oil of Olay and Clearasil families of skin care products.

RVI's international business is still another important asset. In addition to well-respected and established leadership brands internationally, Richardson-Vicks has an experienced organization to market those brands. With products sold in more than 100 countries, RVI will provide a base for further international expansion of P&G products.

Vision and Values

RVI is a company of vision and values with principles and a corporate philosophy very similar to P&G's. It does business with the highest standards of integrity and concern for the quality and safety of its products.

Richardson-Vicks brings to P&G an organization of top-notch people with great depth and experience. Already there is an exciting synergy of P&G and RVI people meshing skills and sharing learning to forge a new era for both companies.



Bethesda-MGM employees gather
outside MGM's international headquarters in
William, Connecticut.





For Beautiful Skin and Hair

P&G and Richardson-Vicks each possess a wealth of knowledge in the area of skin and hair care. This acquisition has placed Procter & Gamble among the world's leading experts in these areas. Combining the capabilities of P&G and RVI particularly in research and marketing, opens potential for dynamic growth.

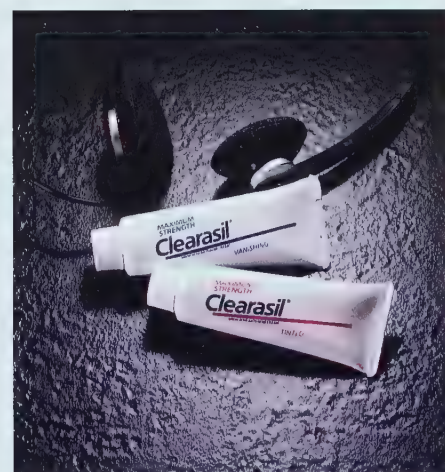
Skin Care

Years of product and marketing excellence have gone into RVI's Oil of Olay, the world's leading skin moisturizer. Its heritage as one of the best known and most-trusted names in skin care has now led to a family of specialty skin care products. Olay's new products, such as the Beauty Bar, Beauty Cleanser, and most recently, Oil of Olay Beauty Cream, have been attracting new users and building the Olay business.

Another winning family of RVI skin care products is Clearasil, the number-one acne care product around the globe.



The newest product to join the Olay family is a new Beauty Cream.





Vidal Sassoon's mousses and styling products are a part of the fastest growing category in health and beauty aids



Hair Care

The RVI acquisition also brought to P&G the Vidal Sassoon and Pantene lines of hair care products. Vidal Sassoon is widely known for bringing the leading trends in hair fashion to consumers.

Pantene is a well-established brand in much of the world and is especially strong in Europe. In the U.S., Pantene is sold mainly in department stores and is expanding to drug and mass merchandising outlets.

The success of P&G's hair care products — Head & Shoulders, Prell, Pert, Ivory and Lilt — reflects advanced research and marketing skills. These P&G strengths can also contribute to the Vidal Sassoon and Pantene businesses.

The resources of both P&G and RVI in the hair and skin care fields promise future success for existing brands, as well as brands yet to come.



Colds Care Experts

With Richardson-Vicks, P&G has gained proven resources in the health care area. RVI researchers have been using their skills to develop the products on demand of relief for cold sufferers around the world. Products such as NyQuil, Formula 44 cough syrup, Vicks Vapoal drops and Airclear are among consumers' favorite cough and cold medicines.

Quality products offering relief from colds have always been the cornerstone of RVI's business. Beginning in 1890 with Vicks Vapoal, the company's oldest brand, Vapoal is one of the world's most widely recognized cold products, sold in almost every country. And even established brands such as Vapoal are continually being re-evaluated and improved to stimulate growth.



A portion of the Vicks research center in Shelton, Connecticut, analyzes how quickly a drug dissolves in solution.



The opportunities for growth in the health care product category are many. RVL researchers are exploring how the growing old can be treated in the future and new products are continually being tested. A trend toward self-medication and use of over-the-counter drugs is dominating in today's increasingly more independent lifestyles. And as the population ages, the demand for health care products rises as well.

P&G increased its presence in the growing health care marketplace in 1992 by acquiring Norwalk Laboratories, a manufacturer with brands such as Euphrasol and Glauconoptic, and in 1993 by purchasing Melanox Laboratories and Key Hol from J. D. Seale. Combining the breadth of experience Norwalk has in pharmaceuticals with RVL's expertise in over-the-counter drugs should accelerate future growth in health care products and fuel P&G's business.

RVL's research portfolio includes a number of over-the-counter and prescription products. RVL's OTC portfolio includes a number of over-the-counter products.







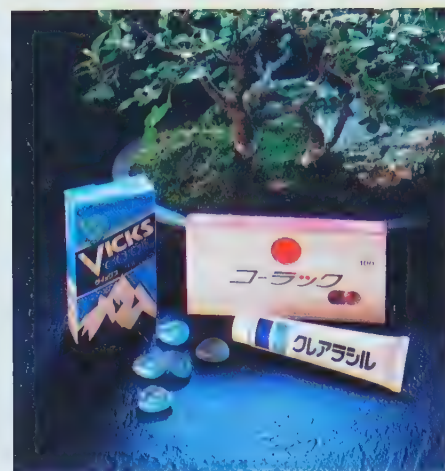
International Strength

Richardson/Vicks brands are market leaders overseas as well as in the U.S. More than half of RVI's profits have come from its international business. This success stems from a wide variety of quality products and an efficient sales and distribution system.

Like P&G, RVI does business in most major international markets, such as Europe and Japan, with a strongly established presence in pharmacies and drug outlets.

In addition, Richardson/Vicks is firmly established in many places where P&G is currently represented or is not yet a major force. In these markets the RVI organization provides a means to introduce P&G products and build the business.

Vicks VapoRub is a registered trademark of P&G. The Richardson/Vicks logo is a trademark of Richardson/Vicks.



*Procter & Gamble's Personal Care Division
is a leader in the industry.*

Procter & Gamble is placing the highest priority on adding advanced technology to share technology with RVI, particularly in the areas of health, skin and hair care.

P&G is a major force in the health and personal care categories because of the strength of brands such as Crest, Clearasil, Pre-Ak-Sol, Mucinex, OTC and the RVI market leaders. P&G is now the largest manufacturer of over-the-counter drugs in the U.S.

With the addition of Richardson-Vicks, Procter & Gamble is forging an exciting future built on our commitment to long-term growth and production of product and marketing innovation.





Millions of Dollars Except Per Share Amounts

	1986	1985	1984
INCOME			
Net sales	\$15,439	\$13,552	\$12,946
Interest and other income	127	193	179
	15,566	13,745	13,125
COSTS AND EXPENSES			
Cost of products sold	9,829	9,099	8,533
Marketing, administrative, and other expenses	4,305	3,477	3,026
Interest expense	257	165	139
	14,391	12,741	11,698
EARNINGS BEFORE INCOME TAXES	1,175	1,004	1,427
INCOME TAXES	466	369	537
NET EARNINGS	\$ 709	\$ 635	\$ 890

Per Common Share

Net earnings	\$4.20	\$3.80	\$5.35
Average shares outstanding (in millions):			
1986—167.8			
1985—167.2			
1984—166.4			
Dividends	\$2.625	\$2.60	\$2.40

Millions of Dollars

	1986	1985
ASSETS		
CURRENT ASSETS		
Cash	\$ 53	\$ 19
Marketable securities	512	459
Accounts receivable, less allowance for doubtful accounts	1,600	1,205
Inventories	2,039	1,754
Prepaid expenses and other current assets	428	379
	4,632	3,816
PROPERTY, PLANT, AND EQUIPMENT	6,322	5,292
GOODWILL AND OTHER INTANGIBLE ASSETS	1,667	329
OTHER ASSETS	434	246
TOTAL	\$13,055	\$9,683

LIABILITIES AND SHAREHOLDERS' EQUITY

CURRENT LIABILITIES		
Accounts payable—trade	\$ 1,108	\$ 981
Accounts payable—other	308	250
Accrued liabilities	1,098	740
Taxes payable	247	219
Debt due within one year	762	399
	3,523	2,589
LONG-TERM DEBT	2,457	877
DEFERRED INCOME TAXES	1,121	945
SHAREHOLDERS' EQUITY		
Preferred stock	250	—
Common stock	168	167
Additional paid-in capital	374	328
Currency translation adjustments	(158)	(293)
Retained earnings	5,320	5,070
	5,954	5,272
TOTAL	\$13,055	\$9,683

Consolidated Statement Of Changes in Financial Position and Consolidated Statement Of Retained Earnings

The Procter & Gamble Company And Subsidiaries **27**
Years Ended June 30, 1986, 1985 and 1984

Millions of Dollars

Consolidated Statement Of Changes in Financial Position

	1986	1985	1984
SOURCE OF FUNDS			
Net earnings	\$ 709	\$ 635	\$ 890
Depreciation, depletion and amortization	491	378	363
Deferred income taxes	213	61	155
Total from operations	1,413	1,074	1,408
Additions to long-term debt	1,562	299	165
Increase in payables and accrued liabilities	216	176	167
Issuance of preferred stock	250	—	—
	3,441	1,549	1,740
USE OF FUNDS			
Capital expenditures	1,069	1,122	906
Dividends to shareholders	445	435	399
Reduction of long-term debt	114	52	318
Increase in inventories	69	214	131
Increase in accounts receivable	28	147	193
Decrease in debt due within one year	6	(42)	(131)
Acquisitions — see Note 2	1,532	—	—
Other items, net	91	(116)	123
	3,354	1,812	1,939
INCREASE (DECREASE) IN CASH AND MARKETABLE SECURITIES	\$ 87	\$ (263)	\$ (199)

Consolidated Statement Of Retained Earnings

	1986	1985	1984
Balance at beginning of year	\$5,070	\$4,879	\$4,420
Net earnings	709	635	890
Dividends to shareholders			
Common	(440)	(435)	(399)
Preferred	(5)	—	—
Excess of cost over the stated value of common shares purchased for treasury	(14)	(9)	(32)
Balance at end of year	\$5,320	\$5,070	\$4,879

1. Summary of Significant Accounting Policies

PRINCIPLES OF CONSOLIDATION: The financial statements include the accounts of The Procter & Gamble Company and its majority-owned subsidiaries. Investments in 20% to 50% owned affiliates in which significant management control is exercised are included at original cost adjusted for the change in equity since acquisition. Other investments in affiliates are carried at cost.

CURRENCY TRANSLATION: Assets and liabilities denominated in most foreign currencies are translated into U.S. dollars at year-end exchange rates and related gains and losses are reflected in shareholders' equity. Gains and losses from foreign currency transactions and translation adjustments in highly inflationary economies are reflected in earnings.

MARKETABLE SECURITIES: Substantially all of the marketable securities are government and corporate debt instruments which are carried at cost which approximates market.

INVENTORY VALUATION: Inventories are valued at the lower of cost or market. Cost for most inventories is determined by the last-in, first-out method. For the remaining inventories, cost is determined primarily by the average cost method.

Futures contracts are purchased primarily to hedge certain agricultural commodity requirements. Gains and losses on these contracts are included in earnings when the related products are sold.

GOODWILL: The excess of the purchase price over the value ascribed to net assets of businesses acquired after October 31, 1970 is amortized on a straight-line basis over forty years. Goodwill arising prior to that date is not amortized.

DEPRECIATION: For financial accounting purposes, depreciation is calculated principally on a straight-line basis over the estimated useful lives of the properties.

INCOME TAXES: Provision is made for the income tax effects of all transactions in the consolidated statement of earnings, including those for which actual tax payment or tax relief is deferred to future years. These deferrals result primarily from the use of shorter equipment lives and accelerated methods of depreciation for tax purposes.

Investment tax credits are recognized as a reduction of the tax expense in the year in which the related assets are placed in service or earlier where permitted by tax regulations.

OTHER EXPENSES: Advertising and research and development costs are charged against earnings in the year incurred.

2. Acquisitions

In November, 1985, the Company acquired Richardson-Vicks Inc., a worldwide manufacturer and marketer of personal care products, for \$1,220 million. In December, 1985, the Company purchased the worldwide over-the-counter drug business of G.D. Searle & Co. for \$312 million. Acquired goodwill, estimated to be \$761 million for both acquisitions, will be amortized over forty years. The full year effect of the acquisitions on consolidated earnings for the current or the previous fiscal year would not have been material.

Earnings Statement Information

The following information is provided for years ended June 30:

Millions of Dollars Except Per Share Amounts	1986	1985	1984
RESEARCH AND DEVELOPMENT COSTS	\$ 479	\$ 400	\$ 369
CAPITALIZED INTEREST	29	37	10
EARNINGS BEFORE INCOME TAXES			
U.S.	936	878	1,255
International	239	126	172
INCOME TAXES			
Current			
Federal	166	240	289
Foreign	72	55	76
Other	15	13	17
	253	308	382
Deferred			
Federal	185	49	140
Foreign and Other	28	12	15
	213	61	155
Deferred tax components:			
Depreciation	155	130	123
Foreign source income and expense	(13)	(37)	50
Other	71	(32)	(18)
	213	61	155
U.S. INVESTMENT, RESEARCH AND ENERGY TAX CREDITS	68	60	48
TOTAL TAX EXPENSE including income taxes identified separately on the consolidated statement of earnings as well as property, franchise, social security, and other taxes paid to federal, state and local governments throughout the world which are included in other cost and expense categories.	755	614	772

THE EFFECTIVE INCOME TAX RATE was 39.7% in 1986, 36.8% in 1985 and 37.6% in 1984, compared to the U.S. statutory tax rate of 46%. U.S. investment, research and energy tax credits accounted for 5.8%, 6.0% and 3.4% in those years. Lower tax rates on our International business, including the effects of subsidiary restructuring, accounted for 3.4% and 3.7% in 1985 and 1984, respectively.

GAINS (LOSSES) FROM CHANGES IN CURRENCY EXCHANGE RATES which are included in net earnings amounted, in millions, to \$33 in 1986, \$(5) in 1985, and \$3 in 1984.

QUARTERLY RESULTS (UNAUDITED)

Quarter Ended	Net Sales		Net Earnings		Per Share of Common Stock			
					Net Earnings		Dividends	
	1985-86	1984-85	1985-86	1984-85	1985-86	1984-85	1985-86	1984-85
September 30	\$ 3,605	\$ 3,485	\$ 250	\$ 223	\$ 1.49	\$ 1.34	\$.650	\$.65
December 31	3,865	3,375	165	137	.99	.81	.650	.65
March 31	4,081	3,350	167	160	.98	.96	.650	.65
June 30	3,888	3,342	127	115	.74	.69	.675	.65
Total Year	\$15,439	\$13,552	\$ 709	\$ 635	\$ 4.20	\$ 3.80	\$ 2.625	\$ 2.60

4. Balance Sheet Information

The following information is provided as of June 30:

Millions of Dollars	1986	1985
INVENTORIES		
Raw materials and supplies	\$ 782	\$ 689
Work in process	204	233
Finished products	1,053	832
	2,039	1,754
Excess of replacement cost over the stated value of LIFO inventories	196	295
PROPERTY, PLANT, AND EQUIPMENT		
Buildings	1,387	1,114
Machinery and equipment	7,228	6,082
Land	174	118
Timberlands, less depletion	161	152
	8,950	7,466
Less accumulated depreciation	2,628	2,174
	6,322	5,292
GOODWILL AND OTHER INTANGIBLE ASSETS	1,744	372
Less accumulated amortization	77	43
	1,667	329
ACCRUED LIABILITIES		
Compensation expenses	176	146
Marketing expenses	380	376
Other	542	218
	1,098	740
LONG-TERM DEBT		
10% sinking fund debentures due 2015	300	—
8% sinking fund debentures due 2016	298	—
9½% notes due 1998	200	—
8¼% sinking fund debentures due 2005	178	178
9% notes due 1992	153	—
6% Japanese yen notes, due 1991	152	—
6% Japanese yen notes due 1992	152	98
10% notes due 1995	150	—
9% notes due 2001	150	—
11% notes due 1989	130	—
8.6% Japanese yen debentures due 1987-1993	122	80
10% notes due 1987, extendible to 1994	65	150
Other, due in varying amounts through 2019	442	397
	2,492	903
Less amounts included in debt due within one year	(35)	(26)
Total long-term debt	2,457	877

Total long-term debt, in millions, amounted to \$630 in 1984; \$783 in 1983; \$846 in 1982.

The following payments, in millions, are required during the next five fiscal years:
1987 — \$35; 1988 — \$125; 1989 — \$24; 1990 — \$188; 1991 — \$212.

Shareholders' Equity

PREFERRED STOCK

Authorized preferred stock is 500,000,000 shares of \$100 par value each. In February, 1986, 2,500,000 variable rate preferred shares were initially offered and were outstanding at June 30, 1986.

COMMON STOCK

Authorized common stock is 500,000,000 shares (without par value) with stated value of \$1 per share. There were 168,266,487, 167,428,920, 166,985,865 and 165,770,054 shares outstanding at June 30, 1986, 1985, 1984, and 1983, respectively, after deducting 1,014,424, 1,507,705, 1,713,374, and 1,316,927 shares held in Treasury at those dates.

Under the Company's stock option plans, options have been granted to key employees to purchase common shares of the Company at the market value on the dates of the grants. Activity for the year ended June 30, 1986 was as follows:

	Shares	Average Price
Outstanding at beginning of year	4,634,595	\$47.01
Options granted	1,269,110	67.38
Options exercised	(1,021,113)	44.65
Options canceled	(131,100)	48.97
Outstanding at end of year	4,751,492	52.90

Options for 3,307,240 shares were exercisable at June 30, 1986. There were 3,251,730 shares available for the granting of options at that date.

ADDITIONAL PAID-IN CAPITAL

Changes in additional paid-in capital for the years ended June 30 are as follows:

Millions of Dollars	1986	1985	1984
Excess amount realized over the stated value of:			
Common shares issued in exchange for \$100 million principal amount of long-term debt (1,423,573 shares in 1984)	\$ —	\$ —	\$ 69
Common shares issued pursuant to employee stock option and remuneration plans (1,053,920, 655,121 and 481,040 shares, respectively, including 709,634, 417,735 and 292,355 treasury shares, respectively)	52	29	19
Expenses related to increase in authorized common and preferred shares and to issuance of preferred shares	(6)	—	—
Total change for the year	\$ 46	\$ 29	\$ 88

CURRENCY TRANSLATION ADJUSTMENTS credited to shareholders' equity, in millions, amounted to \$135, \$(28) and \$(69) for the years ended June 30, 1986, 1985 and 1984, respectively.

Retirement Plans

Most employees are covered by Company funded defined contribution profit sharing plans which provide retirement benefits. Company contributions are based on a percentage of earnings, not to exceed 15% of the salaries and wages of participants, and amounted to \$180 million in 1986 and \$165 million in 1985. Other employees, primarily outside the U.S., are covered by local pension or retirement plans.

Certain health care and life insurance benefits are provided for many retired employees. The cost of these benefits is charged against earnings in the year the claims and premiums are paid. This cost amounted to \$9 million in 1986 and \$10 million in 1985.

7. Segment Information

Sales between geographic areas and those between business segments, included in net sales below, are made at prices approximating market and are eliminated from total net sales. Corporate earnings include interest income and expense, and other general corporate income and expense. Corporate assets include primarily cash and marketable securities.

GEOGRAPHIC AREAS

The Company's international operations are conducted in various countries primarily through self-contained subsidiaries. Each country has a distinct social, political, economic and business environment. No individual country accounts for 10% of consolidated sales or assets.

Millions of Dollars	United States	International	Corporate	Total
<u>Net Sales</u>				
1984	\$ 9,554	\$3,737	\$ (345)	\$12,946
1985	10,243	3,625	(316)	13,552
1986	11,210	4,490	(261)	15,439
<u>Net Earnings</u>				
1984	707	125	58	890
1985	521	96	18	635
1986	634	143	(68)	709
<u>Assets*</u>				
1984	6,072	1,740	1,086	8,898
1985	6,829	1,946	908	9,683
1986	8,394	3,461	1,200	13,055

*Total assets, in millions, amounted to \$8,135 in 1983 and \$7,510 in 1982.

BUSINESS SEGMENTS

The Company's operations are characterized by interrelated raw materials and manufacturing facilities and centralized research and administrative staff functions, making any separate profit determination by product category dependent upon necessarily arbitrary assumptions as to allocations of common costs. Different assumptions or physical or organizational arrangements would produce different results.

Millions of Dollars	Product Categories				Corporate	Total
	Laundry and Cleaning	Personal Care	Food and Beverage	Other		
<u>Net Sales</u>						
1984	\$4,715	\$4,930	\$2,461	\$1,309	\$(469)	\$12,946
1985	4,884	5,107	2,815	1,237	(491)	13,552
1986	5,348	6,451	2,923	1,161	(444)	15,439
<u>Earnings Before Income Taxes</u>						
1984	740	689	(91)	96	(7)	1,427
1985	691	332	(110)	104	(13)	1,004
1986	667	625	(64)	74	(127)	1,175
<u>Assets</u>						
1984	1,845	3,242	1,556	1,169	1,086	8,898
1985	2,038	3,776	1,717	1,244	908	9,683
1986	2,369	6,446	1,761	1,279	1,200	13,055
<u>Capital Expenditures</u>						
1984	228	321	234	113	10	906
1985	216	594	165	110	37	1,122
1986	233	539	157	108	32	1,069
<u>Depreciation and Amortization</u>						
1984	75	149	51	64	24	363
1985	79	165	64	69	1	378
1986	99	243	72	74	3	491

**Segment
Information
(Cont.)**

Laundry and Cleaning Products include detergents, fabric softeners, cleaners and cleansers. Personal Care Products include bar soaps, toothpastes, mouthwash, deodorants, hair care products, skin care products, paper tissue products, disposable diapers, cough/cold remedies and other pharmaceuticals. Sales of disposable diapers represented approximately 16%, 15% and 16% of consolidated sales in 1986, 1985 and 1984, respectively. Food and Beverage Products include shortenings, oils, prepared baking mixes, peanut butter, potato chips, coffee, soft drinks and citrus products. Products of the Laundry and Cleaning, Personal Care and Food and Beverage Products segments are distributed primarily through grocery stores and other retail outlets. Other Products include cellulose pulp and chemicals which are sold direct to customers and through jobbers. Net sales of Other Products include intersegment sales amounting, in millions, to \$436 in 1986, \$490 in 1985 and \$467 in 1984.

**Supplemental
Information on the
Effects of Inflation
and Changing Costs
(Unaudited)**

Information concerning the effects of inflation and changing costs is presented on page 37.

Report of Independent Accountants

**Deloitte
Haskins + Sells**

250 East Fifth Street
Cincinnati, Ohio 45202

To the Board of Directors and Shareholders of The Procter & Gamble Company:

We have examined the consolidated balance sheets of The Procter & Gamble Company and subsidiaries as of June 30, 1986 and 1985 and the related consolidated statements of earnings, retained earnings, and changes in financial position for each of the three years in the period ended June 30, 1986. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the financial statements referred to above present fairly the financial position of the companies at June 30, 1986 and 1985 and the results of their operations and the changes in their financial position for each of the three years in the period ended June 30, 1986, in conformity with generally accepted accounting principles applied on a consistent basis.

Deloitte Haskins + Sells

August 8, 1986

Financial Review 1971-1986 and Analysis And Discussion

Financial Review 1971-1986

	1971	1972	1973	1974
NET SALES	\$3,178	\$3,514	\$3,907	\$4,912
NET EARNINGS	\$ 237	\$ 276	\$ 301	\$ 316
NET EARNINGS PER COMMON SHARE	\$ 1.45	\$ 1.68	\$ 1.84	\$ 1.92
NET EARNINGS AS PERCENT OF NET SALES	7.5%	7.8%	7.7%	6.4%
DIVIDENDS PER COMMON SHARE	\$.70	\$.75	\$.78	\$.90

*Excludes an extraordinary charge of \$75 million (\$.45 per common share) associated with the suspension of sale of Rely tampons.

Net earnings and dividends per common share have been adjusted for the stock split in 1983.

Analysis And Discussion

1986

In November, 1985, Richardson-Vicks Inc., a worldwide manufacturer and marketer of personal care products, was acquired for \$1.2 billion. In December, 1985, the Company acquired the over-the-counter drug business of G. D. Searle & Co. for \$312 million.

Net sales in 1986 increased 14 percent over those for 1985. The increase was primarily due to higher volume, importantly including the addition of the Richardson-Vicks business.

Interest and other income decreased \$66 million principally as a result of a smaller portfolio of marketable securities, and interest expense increased \$92 million primarily due to the higher levels of debt associated with the acquisitions.

Net earnings in 1986 increased 12 percent over those for 1985. The growth in net earnings was held back by both a higher effective income tax rate than in the previous year and the initial dilution effect of two major acquisitions.

Domestic net earnings from operations amounted to \$634 million, a 22 percent increase over the previous year. There was significant growth in the disposable diaper, dentifrice, and liquid laundry detergent categories which form a major part of the domestic business.

Net earnings from international operations amounted to \$143 million, an increase of 49 percent over the previous year. The increase was principally due to the addition of the Richardson-Vicks international business, although existing business growth and currency exchange rates were also positive factors.

1985

Net sales in 1985 increased 5 percent over those for 1984. The increase was primarily due to greater unit volume.

Interest and other income in 1984 included a \$30 million non-taxable gain resulting from exchanges of newly issued common shares for the Company's long-term debt. There was no such gain in 1985.

Millions of Dollars Except Per Share Amounts

1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986
\$6,082	\$6,513	\$7,284	\$8,100	\$9,329	\$10,772	\$11,416	\$11,994	\$12,452	\$12,946	\$13,552	\$15,439
\$ 332	\$ 400	\$ 460	\$ 510	\$ 575	\$ 640	\$ 668*	\$ 777	\$ 866	\$ 890	\$ 635	\$ 709
\$ 2.02	\$ 2.42	\$ 2.78	\$ 3.09	\$ 3.48	\$ 3.87	\$ 4.04*	\$ 4.69	\$ 5.22	\$ 5.35	\$ 3.80	\$ 4.20
5.5%	6.1%	6.3%	6.3%	6.2%	5.9%	5.9%*	6.5%	7.0%	6.9%	4.7%	4.6%
\$.95	\$ 1.03	\$ 1.20	\$ 1.35	\$ 1.55	\$ 1.70	\$ 1.90	\$ 2.05	\$ 2.25	\$ 2.40	\$ 2.60	\$ 2.625

Net earnings were 29 percent lower than in 1984.

Domestic net earnings from operations amounted to \$521 million, a 26 percent decline compared with the previous year. Continued heavy investment in new products expanded nationally over the past two years, as well as costs associated with the launch of the new shaped Pampers disposable diaper, were primarily responsible for the decline in earnings. Profit on the established business — other than diapers — was ahead of 1984.

Net earnings from international operations amounted to \$96 million, a decrease of 23 percent from the previous year. The adverse effect of currency exchange rates, which accounted for over one-half of the decline, and record levels of new business investment combined to depress earnings.

Financial Condition

The Company's financial condition remains very strong despite a significant increase in debt this past year, principally associated with the acquisitions for cash of Richardson-Vicks and the Searle over-the-counter drug business. Total borrowing outstanding at June 30, 1986 was \$3,219 million, compared with \$1,276 million at the end of fiscal 1985. The Company's debt as a percent of capital employed increased to 31% at year-end 1986, compared to 17% at year-end 1985. While this is a significant increase, the Company retains an excellent credit rating which provides broad financial flexibility. In addition to increasing debt, the Company raised additional capital by a new variable rate preferred stock issue amounting to \$250 million.

Cash generated from the Company's operations provided the principal source of funds for the working capital requirements and the capital expenditures that support the growth of the business, and dividends to shareholders. The Company expects to continue financing most of its cash requirements through internally generated funds.

**Financial
Condition
(Cont.)**

The investment in receivables and inventories, less payables and accrued liabilities, amounted to \$878 million as of June 30, 1986. This represents an increase of \$109 million during the year, due primarily to the addition of the newly acquired businesses.

Capital expenditures during the year were \$1,069 million, a decrease of \$53 million from the previous year. During the three year period 1984 through 1986 capital expenditures have totaled \$3,097 million.

Dividends of \$2.625 per common share, \$440 million in total, were paid during the year. The comparable amount for the previous year was \$2.60. This marked the thirtieth consecutive fiscal year of increased dividend payments. Over the three year period 1984 through 1986 dividends have totaled \$1,274 million.

The Company finances its operations outside the United States primarily in local currencies. This acts as a hedge against foreign currency exchange rate changes and minimizes the impact of currency fluctuations on the financial position of the Company. There are no significant restrictions on remittances of funds generated by the Company's operations outside the United States.

Information concerning the effects of inflation and changing costs is presented on page 37.

Responsibility For The Financial Statements

The financial statements of The Procter & Gamble Company and its subsidiaries are the responsibility of, and have been prepared by, the Company, in accordance with generally accepted accounting principles. To help insure the accuracy and integrity of its financial data, the Company has developed and maintains internal accounting controls which are designed to provide reasonable assurances that transactions are executed as authorized and accurately recorded, and that assets are properly safeguarded. These controls are monitored by an extensive program of internal audits.

The financial statements have been examined by the Company's independent public accountants, Deloitte Haskins & Sells. Their report is shown on page 33.

The Board of Directors has an Audit Committee composed entirely of outside Directors. The Committee meets periodically with representatives of Deloitte Haskins & Sells and financial management to review accounting, control, auditing, and financial reporting matters. To help assure the independence of the public accountants, Deloitte Haskins & Sells regularly meets privately with the Audit Committee.

The following table illustrates the impact of inflation on certain charges against the Company's reported earnings, and on the assets from which these charges were derived. Depreciation expense and cost of products sold are restated to a "current cost" basis to arrive at a current cost net earnings. Prior years' current cost and reported earnings as well as other financial indicators such as net sales, dividends per common share and market price per common share at June 30 are restated upward to an average 1985-86 dollar basis, using the U.S. consumer price index.

Shareholders are cautioned that these restated figures are experimental approximations which don't measure fully all of the effects of inflation on the Company's business. Nevertheless, they do indicate the increasing cost of replacing assets during inflationary times. For example, in the latest fiscal year ended June 30, 1986, current cost earnings of \$553 million are lower than reported earnings of \$709 million. The difference is due primarily to \$182 million of additional depreciation expense.

Comparison Of Selected Financial Information — Stated in 1985-86 Dollars

Millions of Dollars Except Per Share Amounts	Year Ended June 30				1986
	1982	1983	1984	1985	
Net Sales	\$13,868	\$13,803	\$13,841	\$13,946	\$15,439
Current cost net earnings	660	747	722	485	553
Inflation gain on net amounts owed ^(a)	131	82	82	84	60
Current cost net earnings per common share	3.99	4.50	4.34	2.90	3.27
Dividends per common share	2.37	2.49	2.57	2.68	2.63
Market price per common share at June 30	46.55	60.28	54.95	56.89	79.66
Net assets at June 30 ^(b)	8,205	8,337	8,716	8,407	8,753
Increase in current costs greater (less) than increase in general inflation ^(b)	(12)	(184)	30	(410)	(236)
Changes in currency translation adjustments	(1)	(113)	(71)	(28)	148
Average U.S. Consumer Price Index	100.0	104.3	108.1	112.4	115.6

(a) The "inflation gain on net amounts owed" provides a general dimension of the benefit to the Company from future payment of its debt in dollars of reduced purchasing power due to continuing inflation.

(b) At June 30, 1986, the current cost of property, plant, and equipment, net of accumulated depreciation, was \$8,970 million and the current cost of inventories was \$2,270 million.

The current cost of property, plant, and equipment was determined from the Company's domestic cost index, or comparable foreign indices, applied by year of asset acquisition. The current cost of inventories was based on current market or receipt prices of materials and current manufacturing expenses. General inflation was measured by consumer price indices in the United States and abroad.

Shareholders' Information

Shareholder Records

The Procter & Gamble Company Stock Transfer Department, P.O. Box 599, Cincinnati, Ohio 45201 maintains all shareholder records and can answer questions regarding shareholders' accounts. Shareholders wishing to transfer stock or to change the name on a stock certificate should contact the Department for instructions.

Stock certificates are valuable and should be safeguarded since replacement takes time and requires a security bond payment by the shareholder. If a stock certificate is lost, stolen or destroyed, the Stock Transfer Department should be notified promptly. Advice for mailing certificates may be obtained from the Department.

Dividend Reinvestment Plan

A Dividend Reinvestment Plan, with a cash payment option, is available to holders of common stock who wish to increase their investment in Procter & Gamble. The Company pays the administrative costs related to the plan. Plan participation is voluntary; and shareholders may join or withdraw at any time.

Full details about the plan are available from:

The Procter & Gamble Company
Stock Transfer Department
P.O. Box 599
Cincinnati, Ohio 45201

Toll Free Telephone Number

A special toll free 800-line is available to answer shareholders' questions about their accounts, dividend checks, dividend reinvestment, stock transfers or related Company subjects. Shareholders outside Ohio should call 1-800-742-6253. Ohio shareholders should call 1-800-582-2685.

Shareholders' Meeting

The next annual meeting of the shareholders will be held on Tuesday, October 14, 1986, at the Company's General Offices, Two Procter & Gamble Plaza, Cincinnati, Ohio 45202.

Corporate Responsibility

Shareholders may receive the booklet "Beliefs Into Actions" which examines key principles guiding Procter & Gamble's social responsibility, and shows how these principles are being put into action. Requests should be sent to: Mrs. Rita M. Neago, Assistant Secretary, The Procter & Gamble Company, P. O. Box 599, Cincinnati, Ohio 45201.

Transfer Agent The Procter & Gamble Company
Stock Transfer Department
P.O. Box 599
Cincinnati, Ohio 45201

Registrar The Central Trust Company, N.A.
5th and Main Sts.
Cincinnati, Ohio 45202

Exchange Listing New York, Cincinnati, Amsterdam, Paris, Basle, Geneva, Lausanne, Zurich, Frankfurt, Antwerp, Brussels, Tokyo.

Price Range The quarterly price range of common shares based on the NYSE-Composite transactions is shown below:

Quarter Ended	1985-86		1984-85	
	High	Low	High	Low
September 30	59.38	55.50	57.63	51.38
December 31	71.75	55.00	59.88	53.00
March 31	76.88	63.75	57.88	54.50
June 30	80.63	71.13	57.00	50.38

Shareholders of Common Stock There were 97,975 shareholders of common stock of record as of July 18, 1986.

Form 10-K Shareholders may obtain in October, 1986 a copy of the Company's 1986 report to the Securities and Exchange Commission on Form 10-K by sending a request to:
Mrs. Rita M. Neago, Assistant Secretary, The Procter & Gamble Company, P.O. Box 599, Cincinnati, Ohio 45201.

